In the Supreme Court of the United States

OCTOBER TERM, 1971.

No. 71-1316

EMORY K. CRENSHAW, as Executor
of the Estate of Frances Wood Wilson, Deceased,
Petitioner,

vs.

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR A WRIT OF CERTIORARI
To the United States Court of Appeals
For the Fifth Circuit

HAROLD E. ABRAMS
KILPATRICK, CODY, ROGERS,
McCLATCHEY & REGENSTEIN
1045 Hurt Building
Atlanta, Georgia 30303
Counsel for Petitioner

Of Counsel:

NELSON K. NEIMAN
KILPATRICK, CODY, ROGERS,
McCLATCHEY & REGENSTEIN
1045 Hurt Building
Atlanta, Georgia 30303

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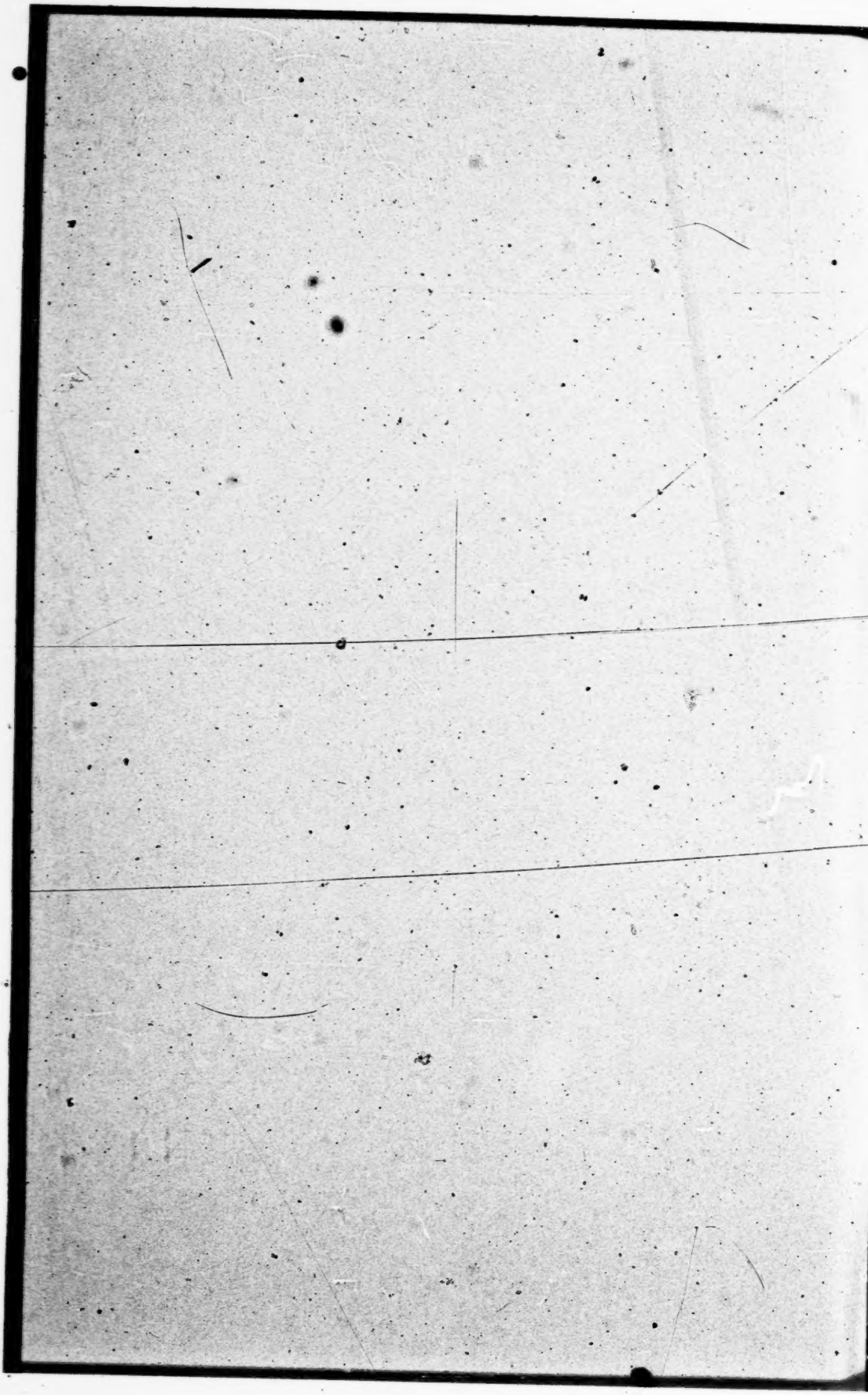

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EMORY K. CRENSHAW, as Executor
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vs.

UNITED STATES OF AMERICA,
Respondent

PETITION FOR A WRIT OF CERTIORARI
To the United States Court of Appeals
For the Fifth Circuit

The Petitioner prays that a writ of certiorari issue to review the opinion of the United States Court of Appeals for the Fifth Circuit dated October 22, 1971, pursuant to which the judgment of the District Court granting the Petitioner's Motion for Summary Judgment was reversed and the cause remanded for entry of judgment in favor of the Respondent. A petition for rehearing was denied on January 14, 1972.

OPINIONS DELIVERED IN THE COURTS BELOW

The opinion of the United States District Court for the Northern District of Georgia granting the Petitioner's Motion for Summary Judgment is reported at 315 F. Supp. 814, and a copy of this opinion is appended hereto at pp. 19 - 26 of the Appendix. The opinion of the Court of Appeals for the Fifth Circuit reversing the District Court and remanding the cause for entry of judgment in favor of the Respondent is not yet reported, but a copy of this opinion is appended hereto at pp. 27 - 36 of the Appendix. A copy of the Court of Appeals' denial of the Petition for Rehearing and a copy of the District Court's Order that the mandate of the Court of Appeals be its judgment are appended hereto at pp. 37 - 38 of the Appendix.

JURISDICTION

The opinion of the Court of Appeals is dated October 22, 1971, and its per curiam denial of the Petitioner's Petition for Rehearing is dated January 14, 1972. On January 27, 1972, the District Court entered an Order that the mandate of the Court of Appeals be the judgment of the District Court, and this Order was filed on January 28, 1972. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

THE QUESTIONS PRESENTED FOR REVIEW

(1) Whether the Court of Appeals erred in holding that Mrs. Frances Wood Wilson did not liquidate her interest in the Pine Forest Associates partnership pursuant to Section 736 of the Internal Revenue Code of 1954 (26 U.S.C. 736), but rather sold that partnership interest pursuant to Section 741 of the Internal Revenue Code of 1954 (26 U.S.C. 741).

(2) Whether the Court of Appeals erred in holding that Mrs. Frances Wood Wilson and the estate of her deceased husband, Fred B. Wilson, did not enter into an exchange of like-kind properties pursuant to Section 1031 of the Internal Revenue Code of 1954 (26 U.S.C. 1031).

(3) Whether the Court of Appeals misconstrued the guidelines of the Supreme Court in *Commissioner v. Court Holding Co.*, 324 U.S. 331 and *United States v. Cumberland Public Service Co.*, 338 U.S. 451, in applying the "substance versus form" doctrine to the transactions under review.

THE STATUTES AND REGULATIONS INVOLVED

The statutes involved are the pertinent portions of sections 731, 736, 741, 761 and 1031 of the Internal Revenue Code of 1954, as amended (26 U.S.C. 731, 736, 741, 761 and 1031). The regulations involved are the pertinent portions of Treas. Reg. §1.736-1(a)(1) and Treas. Reg. §1.1031(a)(1). Such portions of these statutes and regulations are appended hereto at pp. 39-41 of the Appendix.

STATEMENT OF THE CASE

Immediately prior to November 30, 1962, Mrs. Frances Wood Wilson (hereinafter called the "Taxpayer") and Mr. and Mrs. Leon Blair were the three partners in the Pine Forest Associates partnership (hereinafter called the "Partnership"). The Pine Forest Apartments (hereinafter called the "Apartments") were the primary asset of the Partnership, and the Taxpayer owned a 50/225th interest in the Partnership.

Leon Blair informed the Petitioner, who was the Taxpayer's financial advisor, that he would like to purchase the Taxpayer's interest in the Partnership. Blair was advised that the Taxpayer would not dispose of her Partnership interest for cash, but that she would consider withdrawing from the Partnership pursuant to a transaction which would provide her with income producing property. Thereupon, in accordance with a preconceived plan, the following three transactions were entered into on November 30, 1962, in the sequence set forth below:

(a) The Taxpayer completely withdrew from and terminated her interest in the Partnership, receiving for her interest an undivided 50/225th interest in the Apartments owned by the Partnership.

(b) The Taxpayer exchanged her undivided 50/225th interest in the Apartments for the Oglethorpe Shopping Center, which was owned by the estate of her deceased husband, Fred B. Wilson. The Taxpayer was executrix of this estate.

(c) The estate of Fred B. Wilson sold its undivided 50/225th interest in the Apartments to Blair Investment Company for $200,000. All of the issued and outstanding stock of Blair Investment Company was owned by Mr. and Mrs. Leon Blair.

At an unspecified date subsequent to November 30, 1962 and prior to January 31, 1963, Blair Investment Company transferred its undivided 50/225th interest in the Apartments to the Partnership.

The Commissioner of Internal Revenue determined that the Taxpayer disposed of her Partnership interest in a taxable transaction and that she owed an income tax deficiency of $38,518.29 for the year 1962. The alleged deficiency of $47,128.92, including interest, was paid on August 3, 1967, and a claim for refund was filed on April 25, 1968. The claim for refund was disallowed in full, and the Petitioner brought an action in the District Court to recover the income taxes and interest thereon pursuant to the jurisdiction conferred by 28 U.S.C. §1346(a)(1). As indicated above, the District Court granted the Petitioner's Motion for Summary Judgment, and in so doing found that the Taxpayer's Partnership interest was liquidated pursuant to Section 736 and that she then entered into an exchange of like-kind properties with her husband's estate pursuant to Section 1031. Accordingly, the District Court held that such transactions did not result in the recognition of taxable gain. The Court of Appeals reversed the District Court and remanded the cause with the direction that judgment be entered for the Respondent.

REASONS FOR GRANTING THE WRIT

I. In holding that the Taxpayer sold her interest in the Partnership to Blair Investment Company, the Court of Appeals rendered a decision in conflict with a decision of the Court of Appeals for the Third Circuit on the question of when a withdrawing partner liquidates his partnership interest rather than sells that interest to the remaining partners.

In its opinion in the instant case, the Court of Appeals states that "The steps with which we are concerned are those that lead inevitably to a taxable sale, even though individually any one step may have the technical form of a §736 liquidation." It further states,

> "In return for its $200,000 cash payment the corporation (Blair Investment) received exactly the partnership interest it would have obtained by way of a direct purchase from Taxpayer. A sale, not a 'liquidation,' occurred because what had formerly been Taxpayer's partnership interest was acquired by the Blairs' corporate alter ego and the relative economic positions of the parties were the same as they ultimately would have been had a direct sale taken place."

The reasoning and holding of the Court of Appeals cannot be reconciled with either the decision of the Third Circuit in *Foxman v. Commissioner*, 352 F.2d 466 (3rd Cir., 1965), aff'g 41 T.C. 535 (1964) or the mandate of Congress in enacting subchapter K of the Internal Revenue Code. In its opinion in *Foxman*, the Tax Court summarized the legislative intendment behind subchapter K by stating the following:

> "In its report on the bill which became the 1954 Code the House Ways and Means Committee stated that the then 'existing tax treatment of partners and partnerships is among the most confused in the entire

tax field'; that 'partners * * * cannot form, operate, or dissolve a partnership with any assurance as to tax consequences'; that the proposed statutory provisions [subchapter K] represented the 'first comprehensive statutory treatment of partners and partnership in the history of the income tax laws'; and that the 'principal objectives have been simplicity, flexibility, and equity as between the partners.' H. Rept. No. 1337, 83d Cong., 2d Sess., page 65. Like thoughts were expressed in virtually identical language by the Senate Finance Committee. S. Rept. No. 1622, 83d Cong., 2d Sess., page 89.

"Although there can be little doubt that the attempt to achieve 'simplicity' has resulted in utter failure, the new legislation was intended to and in fact did bring into play an element of 'flexibility.' Tax law in respect of partners may often involve a delicate mechanism, for a ruling in favor of one partner may automatically produce adverse consequences to the others. *Accordingly, one of the underlying philosophic objectives of the 1954 Code was to permit the partners themselves to determine their tax burdens inter sese to a certain extent, and this is what the committee reports meant when they referred to 'flexibility.' The theory was that the partners would take their prospective tax liabilities into account in bargaining with one another.*" [41 T.C. at 550-551 (Footnote omitted; Emphasis added).]

Applying this legislative policy of flexibility to the facts before it, the Tax Court said:

"Where the practical differences between a 'sale' and a 'liquidation' are, at most, slight, if they exist at all, and where the tax consequences to the partners can vary greatly, it is in accord with the purpose of the statutory provisions to allow the partners themselves, through arm's-length negotiations, to determine whether to take the 'sale' route or the 'liquidation' route, thereby allocating the tax burden among themselves." (41 T.C. at 551-552)

In the instant case the Taxpayer rejected Leon Blair's offer to purchase her Partnership interest for cash; her financial advisor negotiated a series of transactions whereby the Taxpayer would withdraw from the Partnership via the "liquidation" route; the Taxpayer terminated her entire Partnership interest as required by section 761 and received a distribution from the Partnership; and the documentation surrounding her withdrawal from the Partnership is consistent with these facts. Thus there can be no question but that the partners selected the "liquidation" route pursuant to section 736 rather than the "sale" route pursuant to section 741. In holding that the Taxpayer sold her Partnership interest despite these facts, the Court of Appeals' opinion conflicts sharply with the Third Circuit's decision in *Foxman*. Even more important, it obviates the distinction between sections 736 and 741 and destroys the flexibility which Congress intended in enacting subchapter K.

II. In failing to find that the Taxpayer entered into an exchange of like-kind properties with her husband's estate, the Court of Appeals rendered a decision in conflict both with its own previous decisions and those of other Courts of Appeals on the question of what constitutes a three party exchange of like-kind properties under section 1031.

Under section 1031(a), no gain or loss is recognized if property held for productive use in trade or business or for investment is exchanged solely for property of a like kind to be held either for productive use in trade or business or for investment. In a classic three party exchange under section 1031 (a), A owns property which B wishes to purchase; A designates like-kind property owned by C which A wishes to acquire; and at a simultaneous closing B purchases the property from C and then exchanges it

for the property owned by A. While this Court has never passed on the question of whether there is non-recognition of gain pursuant to a three party exchange, the Courts of Appeals for the Fourth, Fifth and Ninth Circuits, as well as numerous lower courts, have upheld the non-recognition of gain in such an exchange, and the Commissioner has acquiesced in most of these decisions. To the tax practitioner, the use of the three party exchange of like-kind properties has become a planning device which is both widespread and immune from tax when utilized within well defined perimeters. This has been particularly true since the Commissioner acquiesced in the Tax Court's decision in *Leslie Q. Coupe*, 52 T.C. 394, acq. I.R.B. 1970-2 at p. 5. In the instant case, however, regardless of how unwittingly, the Court of Appeals has cast doubt on the validity of all three party exchanges, and in so doing has come in conflict with both its own and with decisions of the Fourth and Ninth Circuits, not to mention the Commissioner's position as indicated by his acquiescence in the *Coupe* case.

In reaching its holding that the Taxpayer sold her interest in the Partnership, the Court of Appeals cited the well established "substance versus form" and "step transaction" doctrines. It then stated:

> "Here the successful application of these principles depends upon a showing by the Government that, while in form these transfers may appear to be no more than a liquidation of a partnership interest followed by a tax-free §1031 exchange, in substance they are really nothing more than a camouflaged sale of a partnership interest masquerading as a liquidation. But in order to reach this conclusion it must be shown that the character of the transaction is in every respect, other than the superficial and irrelevant one of form, a sale, resulting in precisely those consequences that would have occurred had Taxpayer simply sold

her interest in the partnership to the partnership or to the surviving partners for $200,000 cash and then purchased with that money her income-producing property." (Footnote omitted.)

The Court of Appeals' emphasis upon the overall substance of the transactions before it and its utilization of the step transaction doctrine cannot be reconciled with either the decision of the Fourth Circuit in *Coastal Terminals v. United States*, 320 F.2d 333 (4th Cir., 1963) or the decision of the Ninth Circuit in *Alderson v. Commissioner*, 317 F.2d 790 (9th Cir., 1963). Indeed, the Court of Appeals' opinion is in conflict with its own earlier decision in *W. D. Haden v. Commissioner*, 165 F.2d 588 (5th Cir., 1948), the rationale behind its decision in *Carlton v. United States*, 385 F.2d 238 (5th Cir., 1967)[1], and the rationale behind its decision in *Redwing Carriers v. Tomlinson*, 399 F.2d 652 (5th Cir., 1968)[2]. These cases hold that while

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[1] In *Carlton*, in finding that there was no exchange under section 1031 because the taxpayers received cash and an assignment of the contract for the new property in consideration for their ranch rather than the new property itself the Court of Appeals for the Fifth Circuit said:

"In the instant case, while elaborate plans were laid to exchange property, the substance of the transaction was that the appellants received cash for the deed to their ranch property and not another parcel of land. The very essence of an exchange is the transfer of property between owners, while the mark of a sale is the receipt of cash for the property." (385 F.2d at 242)

[2] In *Redwing*, the Court of Appeals for the Fifth Circuit noted that section 1031 is mandatory rather than elective and held that the taxpayers' sale of trucks and corresponding purchase of new ones constituted parts of the same transaction rather than separate ones. In so holding, the Court of Appeals explained the distinction between a sale and repurchase as in *Carlton* and an exchange as in the case before it as follows:

"The appellant would have us follow *Carlton* here as if that case had ignored transactional substance and instead had viewed the whole only as an aggregate of separate, unrelated transfers. On the contrary, in that case we gave

the nature of a three party exchange of like-kind property is such that there must be two pre-planned, complementary and related transactions before the parties are in a posture to consummate the exchange, section 1031(a) affords non-recognition of gain if there is a bona fide transfer of property, notwithstanding the alternative pursuant to which a party can sell his property and then purchase the new property rather than require the purchaser of his property to purchase the new property and then enter into the exchange.

In the instant case, the Blairs offered to purchase the Taxpayer's interest in the Partnership. The Taxpayer refused but said that if she could withdraw from the Partnership and then exchange property received from the Partnership for income producing property, she would be willing to divest herself of any interest in the Partnership. Since, as is almost always true in a three party exchange, the prospective purchaser (Blair Investment Company) did not own suitable income producing property, the Taxpayer found the property which was satisfactory for an exchange. The only distinction between the exchange before this Court and a classic three party exchange as described above is that instead of Blair Investment Company acquiring Oglethorpe Shopping Center for cash and then

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weight to the various individual transfers *only* because they *were* separate and unrelated. In *Carlton* we were reviewing a three-way transaction in which the taxpayer had received, in return for property, cash which was not restricted in use to the purchase of like property. The most that could be said for the transactional relationship in *Carlton* was that the sale for cash between the taxpayer and a purchaser had been *complementary* with the later purchase of like property between the taxpayer and a seller. In the case at bar, however, there were only two parties to each exchange of trucks (ignoring intracorporate fictional distinctions), and the alleged 'sale' and 'trade-in sales,' instead of being separate, were related by contractual interdependency." (399 F.2d at 659)

exchanging the shopping center for the Taxpayer's interest in the Apartments, the first step was the exchange of the shopping center for the Apartments and the second step was the sale of the Apartments for cash. This slight deviation from the classic three party exchange case was approved in *Leslie Q. Coupe, supra*, a case in which the Commissioner acquiesced.

In *Alderson v. Commissioner, supra*, the taxpayers entered into an agreement to sell their farm ("Buena Park") for cash and the purchaser, Alloy, deposited $17,205 in an escrow, to be applied toward the purchase of the property. The taxpayers, however, desired to enter into a like-kind exchange and subsequently found suitable property ("Salinas"). Thereupon, the taxpayers and Alloy amended their agreement to provide that Alloy would purchase the Salinas property and then exchange it for the Buena Park property, and that if the exchange was not consummated by a certain date Alloy would purchase the Buena Park property. The taxpayers deposited $19,000 in the escrow and authorized the escrow agent to convey the Salinas property to Alloy provided a deed from Alloy to the taxpayers could be immediately recorded. At the closing, the escrow agent acquired the Salinas property using the $19,000 deposited by the taxpayers; it conveyed the Salinas property to Alloy; and Alloy then exchanged the Salinas property for the Buena Park property. Based on these facts, the Ninth Circuit concluded that the parties had a plan to exchange properties within the intent of section 1031, and that the acquisition of property by Alloy for the sole purpose of trading it did not transform the exchange, pursuant to which the Salinas and Buena Park properties were transferred for each other, into a sale by the taxpayers of the Buena Park property followed by their purchase of the Salinas property.

Even though the *Alderson* rationale was followed in

Coastal Terminals, Inc. v. United States, supra, the Court of Appeals for the Fifth Circuit has now clearly departed from this precedent in the instant case and created a conflict between itself and the Fourth and Ninth Circuits. It has done so by holding that the Taxpayer and her husband's estate did not enter into a section 1031 exchange even though they intended to enter into an exchange, the Taxpayer transferred her interest in the Apartments and received the Oglethorpe Shopping Center in return, and the Taxpayer did not have even constructive receipt of the cash paid for the Apartments by Blair Investment Company. This Court should grant certiorari to resolve this conflict between the decision of the Court of Appeals in this case and the decisions of the Fourth and Ninth Circuits on the question of what constitutes a three-party exchange of like-kind property, particularly since this tax-planning device is in such widespread use.

III. Certiorari should be granted to review the holding of the Court of Appeals to the effect that the transactions under review constituted a sale by the Taxpayer of her Partnership interest to Blair Investment Company followed by her purchase of the Oglethorpe Shopping Center from her husband's estate, since such holding depends upon an erroneous application of the "substance versus form" doctrine as set forth in Commissioner v. Court Holding Co., supra, and United States v. Cumberland Public Service Co., supra.

In its opinion, the Court of Appeals quoted this Court in *Commissioner v. Court Holding Co.*, 324 U.S. at 334 as follows: "To permit the true nature of a transaction to be disguised by mere formalisms, which exist solely to alter tax liabilities, would seriously impair the effective administration of the tax policies of Congress." In so doing, the Court below ignored *United States v. Cumberland Public*

Service Co., supra, the case in which this Court further clarified the "substance versus form" doctrine and put its decision in *Commissioner v. Court Holding Co.* in proper perspective.

In both the *Court Holding Co.* and *Cumberland Public Service Co.* cases, the issue for determination was whether assets were sold by a corporation prior to its liquidation or by its shareholders after the liquidation. In *Court Holding Co.*, the Tax Court found that the corporation negotiated the sale of its assets and reached an oral agreement to sell, that the sale was cancelled when the tax consequences were recognized, that the assets were distributed to the shareholders as a liquidating dividend, that the shareholders then sold the assets to the same persons on substantially the same terms, and that the whole transaction showed a sale by the corporation rather than the shareholders. This Court affirmed that decision. In *United States v. Cumberland Public Service Co.*, while the shareholders had previously offered to sell their stock in the corporation and the purchaser counter-offered to purchase the assets from the corporation, each of these offers was rejected and the proposal which was accepted was one whereby the shareholders acquired the assets pursuant to a liquidation of the corporation and then sold them to the purchaser. The Court of Claims found that the method used was chosen in order to reduce taxes, but still found that the sale was made by the shareholders rather than the corporation. In affirming the lower court's finding that the shareholders rather than the corporation made the sale, the Supreme Court made the following observations:

> "While the distinction between sales by a corporation as compared with distribution in kind followed by shareholder sales may be particularly shadowy and artificial when the corporation is closely held. Con-

gress has chosen to recognize such a distinction for tax purposes . . . Consequently, a corporation may liquidate or dissolve without subjecting itself to the corporate gains tax, even though a primary motive is to avoid the burden of corporate taxation. The oddities in tax consequences that emerge from the tax provisions here controlling appear to be inherent in the present tax pattern. For a corporation is taxed if it sells all its physical properties and distributes the cash proceeds as liquidating dividends, yet is not taxed if that property is distributed in kind and is then sold by the shareholders. In both instances the interest of the shareholders in the business has been transferred to the purchaser. Again, if these stockholders had succeeded in their original effort to sell all their stock, their interest would have been transferred to the purchasers just as effectively. Yet on such a transaction the corporation would have realized no taxable gain." (338 U.S. at 456)

"Congress having determined that different tax consequences shall flow from different methods by which the shareholders of a closely held corporation may dispose of corporate property, we accept its mandate." (338 U.S. at 454-455)

An application of the guidelines set forth in the *Court Holding Co.* and *Cumberland Public Service Co.* cases makes it abundantly clear that the Court of Appeals has incorrectly applied the "substance versus form" doctrine to the transactions before it. Congress, by enacting section 736, gave a partner withdrawing from a partnership the option of liquidating his partnership interest instead of selling it pursuant to section 741; and it is clear that the choice between these alternative statutory routes can be motivated primarily by the varying tax burdens. Likewise, Congress gave a property owner the alternative of entering into an exchange of like-kind property under section 1031 or selling his property and then purchasing new property with the proceeds; and it is equally clear that the

choice between these routes can be motivated primarily by differing tax consequences. For some reason unexplained except for its erroneous application of the "substance versus form" doctrine, the Court of Appeals has determined that notwithstanding the fact that a party can both liquidate his partnership interest and enter into a like-kind exchange of property primarily for tax reasons, he cannot do both if the net result is equivalent to the sale of his partnership interest. In reaching this holding, the Court of Appeals has not found that the Taxpayer had constructive receipt of the $200,000 paid for the interest in the Apartments; nor that the Taxpayer and her husband's estate were one party. Yet it still holds that the Taxpayer sold her Partnership interest to Blair Investment Company, apparently because ". . . this well-engineered series of exchanges was for all practical purposes substantially the same as it would have been had they chosen the direct rather than the circuitous route." This Court has repeatedly held that a taxpayer has the legal right to decrease the amount of his taxes, or altogether avoid them, so long as the thing done was what the statute intended, *Gregory v. Helvering*, 293 U.S. 465, and *Knetsch v. United States*, 364 U.S. 361; and numerous courts have repeatedly held both that there is a liquidation of a partnership interest under section 736 if the parties so intended and the documents so reflect, and that there is an exchange under section 1031 so long as the parties actually transfer deeds. Although the Court of Appeals was apparently concerned that the Taxpayer has uncovered a tax loophole through her use of two successive non-recognition provisions, a tax loophole created by statute can be closed only by statutory amendment and such a loophole cannot have an impact upon judicial interpretation of that statute. *Hanover Bank, Executor v. Commissioner*, 369 U.S. 672. Thus it must be concluded that the Court of Appeals went beyond both the

guidelines of this Court and the scope of allowable judicial review when it held that there was a sale of the Taxpayer's Partnership interest rather than a distribution of property from the Partnership to her in liquidation of her Partnership interest and a subsequent exchange of such property for like-kind property.

Indeed, the Court of Appeals has, in its opinion in this case, undercut the traditional "form versus substance" concept by its complete reliance for its result upon the formalistic step (iv)—the transfer by Blair Investment Company of its 50/225ths interest in the Apartments to the Partnership in exchange for a Partnership interest. The opinion states:

> "Obviously what happened here was not equivalent to a sale unless the final step (iv) was consummated—that is, unless Mrs. Wilson's undivided 50/225 interest in the Pine Forest Apartments ultimately found its way back into the partnership now owned by the two Blairs.
>
> * * * * *
>
> What does, instead, make the transaction in question a sale is the fact that while theoretically a matter of indifference to Taxpayer, consummation of the step (iv) was practically essential to its success, since without it there might have been no deal."

The Court of Appeals' initial error is that it allows a step admittedly beyond the Taxpayer's control and of no consequence to her to be the deciding factor which causes the Taxpayer to realize taxable gain. Of greater significance is the Court of Appeals' blatant holding that the remainder of the transactions would not have been taxable if the Blairs had kept the 50/225ths interest in the Apartments in their "corporate alter ego." Since the Blairs either directly or through their controlled corporation would have owned or controlled the Partnership and the

Apartments, step (iv) could have been avoided. It certainly follows that the Court of Appeals has allowed form to prevail over substance by sanctioning the same transactions without tax consequences if step (iv) is omitted.

Certiorari should be granted to establish this Court's guidelines both with respect to the substance of a liquidation of a partnership interest under section 736 as opposed to a sale of that interest under section 741 and with respect to an exchange of like-kind property pursuant to section 1031. The decision of the Court of Appeals has created a conflict between itself and the Courts of Appeals of the various other circuits on each of these questions. Likewise, certiorari should be granted to determine whether, as is implied in the opinion of the Court of Appeals, there is either a statutory or judicial prohibition on the use of two successive statutory non-recognition provisions.

CONCLUSION

For the reasons aforesaid, it is respectfully prayed that a writ of certiorari be granted to review the judgment of the United States Court of Appeals for the Fifth Circuit.

Respectfully submitted,

HAROLD E. ABRAMS,
1045 Hurt Building
Atlanta, Georgia 30303
Counsel for Petitioner

APPENDIX

DECISION OF THE DISTRICT COURT

(June 29, 1970)
Civil Action No. 12392

UNITED STATES DISTRICT COURT
N. D. GEORGIA, ATLANTA DIVISION

EMORY K. CRENSHAW and EDGAR LEE NALLEY,
As Executors of the Estate of Frances Wood Wilson, Deceased

vs.

UNITED STATES OF AMERICA.

ORDER

EDENFIELD, *District Judge*.

This is an action against the United States for tax refund in the amount of $47,128.92, representing income tax and accrued interest thereon which allegedly was erroneously and illegally collected by defendant in 1967 from Frances Wood Wilson, now deceased, for the calendar year 1962.

The controversy centers around a transaction in 1962 whereby Frances Wood Wilson disposed of a partnership interest she possessed, receiving in return therefor an interest in certain investment property owned by the partnership. Taxpayer Wilson treated the transaction as a distribution of partnership property in liquidation of her partnership interest, and pursuant to the provisions of Section 731 of the Internal Revenue Code, 26 U.S.C. § 731, recognized no gain on the transaction. The Commissioner of Internal Revenue subsequently determined that the "retirement or disposition of the partnership interest" should be treated as a taxable capital transaction and that taxpayer

therefore owed an income tax deficiency of $38,518.29 for the calendar year 1962. The alleged deficiency of $47,128.92, including interest, was paid by taxpayer on August 3, 1967, and on April 25, 1968, a claim for refund was filed by plaintiffs on behalf of taxpayer's estate. The claim was disallowed in full and this suit resulted. The case is now before the court for consideration of motions for summary judgment by both plaintiffs and defendant.

In order to understand the Government's contention that taxpayer sold or exchanged her partnership interest to the continuing partners, it is necessary to examine—at least to a limited extent—the background and surrounding circumstances of the transaction in question. These facts, like those set forth above, are not disputed, but the parties disagree as to the effect of the series of transactions involved.

In November 1962 taxpayer possessed a 50/225th interest in a partnership known as Pine Forest Associates —a partnership which had been formed in 1952 with four partners but which had been reduced to three partners in May 1968 when partners Frances Wilson, Leon M. Blair, and Julian H. Blair purchased the interest of Martha Wilson for $200,000. Some time prior to November 1962 Leon M. Blair informed taxpayer's financial adviser, Emory K. Crenshaw, that he (Blair) wished to purchase taxpayer's interest in the partnership. Mr. Crenshaw has testified that after thinking about the matter he concluded that it would be to taxpayer's advantage to dispose of the partnership interest but since she had a great deal of cash already the transaction should be one which would provide her with income-producing property instead of cash. Later discussions revealed that Mr. Blair did not have any such property but Mr. Crenshaw learned that a suitable piece of property was then owned by and could be obtained from the estate of taxpayer's husband. After consulting with

taxpayer's attorneys as to how taxpayer could obtain the income-producing property she desired, Mr. Crenshaw proposed to Mr. Blair a method by which Blair could obtain control over taxpayer's partnership interest without purchasing it from taxpayer; the plan was approved and on November 30, 1962, the following individual actions occurred:

(1) Taxpayer withdrew from the Pine Forest Associates partnership, receiving for her interest an undivided 50/225th interest in the real estate owned by the partnership (i.e., Pine Forest Apartments), without liability for payment of any debts, claims or liabilities to which the apartments were subject.

(2) Taxpayer exchanged her undivided 50/225th interest in the Pine Forest Apartments for the Oglethorpe Shopping Center, which was owned by the estate of her deceased husband, Fred B. Wilson.

(3) The estate of Fred B. Wilson then sold the undivided interest in Pine Forest Apartments to Blair Investment Company for $200,000.

(4) Blair Investment Company contributed its interest in Pine Forest Apartments to the Pine Forest Associates partnership and thereby became a partner itself.

The Government concedes that if viewed as a separate transaction the partnership distribution to the taxpayer would be a valid liquidating distribution under §§ 731 and 736(b), and that the subsequent exchange was a valid one, but it contends that the distribution cannot be viewed as a separate transaction; rather, it argues that the foregoing transactions, all of which occurred on the same day, constituted in substance a "sale or exchange" of Frances Wilson's partnership interest, under 26 U.S.C. § 741, rather than a bona fide liquidating distribution under §§ 731 and 736(b), as contended by plaintiffs, and it was on

that basis that nonrecognition of capital gains was disallowed.[1] The Government looks to the end result, finds that at the conclusion of transaction No. 4, *supra*, the partnership was composed of the two continuing partners and a corporation of which those partners were sole shareholders, and that the partnership assets were exactly the same as they had been before taxpayer disposed of her interest. From this the Government concludes that taxpayer's disposition of her interest was, in effect, by way of a sale or exchange to the continuing partners. The court rejects that contention for it completely ignores what this court finds to be the most important factors in determining

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[1] Section 741 of the Internal Revenue Code, 26 U.S.C. § 741, provides as follows:

> "In the case of a sale or exchange of an interest in a partnership, gain or loss shall be recognized to the transferor partner. Such gain or loss shall be considered as gain or loss from the sale or exchange of a capital asset * * * [with one exception which is not relevant to the instant case]."

Section 731 provides in relevant part:

> "(a) Partners.—In the case of a distribution by a partnership to a partner—
>
> (1) gain shall not be recognized to such partner, except to the extent that any *money* distributed exceeds the adjusted basis of such partner's interest in the partnership immediately before the distribution * * * " [Emphasis added.]

Section 736(b) clarifies what is meant by a "distribution by a partnership":

> "Payments made in liquidation of the interest of a retiring partner shall, to the extent such payments * * * are determined, under regulations prescribed by the Secretary or his delegate, to be made in exchange for the interest of such partner in partnership property, be considered as a *distribution by the partnership* * * *." (Emphasis added.)

Section 1.736-1 of the Treasury Regulations on Income Tax (1954 Code), provide further that § 736 applies "only to payments made by the partnership and not to transactions between the parties. Thus, a sale by partner A to partner B of his entire one-fourth interest in partnership ABCD would not come within the scope of section 736."

whether a retiring partner's interest was sold or whether it was liquidated: (1) whether the partner disposed of his entire interest in the partnership,[2] and (2) whether the partners themselves chose to use the "sale route" or the "liquidation route."

[1] In rejecting the Government's contention that taxpayer sold her partnership interest, the court notes that the Government is correct in asserting that it is the substance of a transaction rather than its mere form which is controlling for purposes of taxation. But this statement usually has been made when the court was dealing with a transaction which was itself a sham. For example, in *Gregory v. Helvering,* 293 U.S. 465, 55 S.Ct. 266, 79 L.Ed. 596 (1935), and *Bazley v. Commissioner of Internal Revenue,* 331 U.S. 737, 67 S.Ct. 1489, 91 L.Ed. 1782 (1947)—both of which the Government has cited—the court was faced with taxpayers who claimed the tax benefits flowing from corporate reorganization when the reorganizations themselves were shams entered into not for corporate business purposes but solely to permit shareholders to escape tax liability on otherwise taxable gains. Just as in the foregoing cases the benefits derived from corporate reorganization are dependent upon there being an actual reorganization for business purposes, in cases involving termination of a partnership interest the benefit of deferred recognition of capital gains is dependent upon whether partnership property is transferred to the retiring partner in complete liquidation of that partner's partnership interest. If the taxpayer in some manner retains his partnership interest in substance though not in form then the *Gregory* and *Bazley* decisions are directly in point.

The instant case does not involve reduction or elimina-

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[2] Merten's Law of Federal Income Taxation. *See* Code Commentary, § 731-735: 3.

tion of tax liability but, rather, postponement of tax liability to a later date. Nor does it involve a sham liquidation of a partner's interest. The retiring partner completely disposed of her partnership interest and in exchange therefor she received an interest in property owned by the partnership. True, the partnership itself ended up holding exactly the same properties it had held before, but that is not the determining factor.

Other courts have pointed out that when Congress enacted subchapter K of the 1954 Internal Revenue Code it did so with the idea of achieving simplicity, flexibility, and equity, and that the flexibility which was sought in the area of disposition of a partner's interest contemplated that the partners would determine for themselves whether they wished to take the "sale route" or the "liquidation route." *E. g., Foxman v. Commissioner of Internal Revenue,* 352 F.2d 466 (3d Cir. 1965), aff'g. 41 T.C. 535 (1964). Having clearly chosen one route neither the retiring nor the continuing partners can later lay claim to the tax consequences which would have followed from using the other route.

When the courts have been faced with the problem of determining which route the partners did in fact choose, they uniformly have looked to the agreement which formed the basis of the transaction. *E. g., Foxman v. Commissioner, supra; Kinney v. United States,* 228 F. Supp. 656 (W.D.La.1964), aff'd., 358 F.2d 738 (5th Cir. 1966); *Andrew O. Stilwell v. Commissioner,* 46 T.C. 247 (1966); *Miller v. United States,* 181 Ct.Cl. 331 (1967).

For example, in *Foxman v. Commissioner, supra* (the case upon which defendant relies most heavily in arguing that taxpayer in the instant case sold her interest), the continuing partners contended that the retiring partner had received a partnership distribution in liquidation of his interest, but both the Tax Court and the Court of

Appeals found that the retiring partner had *sold* his interest. The courts noted that the entire tenor of the transaction was that of a sale rather than a liquidation. As the Court of Appeals said:

> "[The members of the partnership] had a choice of means by which [the retiring partner's] withdrawal could be effected. They could have agreed inter se on either liquidation or sale. On a consideration of the plain language of the contract the negotiations which preceded its consummation, the intent of the parties as reflected by their conduct, the circumstances surrounding the transaction, the Tax Court found that the transaction was in substance a sale and not a liquidation of a retiring partner's interest. This finding is amply supported by the evidence in the record. The partners having employed the sale method to achieve their objective, [the continuing partners] cannot avoid the tax consequences by a hind-sight application of principles they now find advantageous to them and disadvantageous to [the retiring partner]."

[2] In the instant case the plain language of the contract indicates that the partners chose the liquidation route to achieve their objectives, although Mr. Blair had indicated a desire to purchase taxpayer's partnership interest, taxpayer had in effect declined to sell and the agreement entered into with regard to taxpayer's retiring from the partnership was one for liquidation of her interest. Subchapter K makes provision for delaying recognition of capital gains with respect to liquidation of a partner's interest, if the partners choose to do so, just as §1031 provides for delayed recognition of gain with regard to an exchange of like-kind property. The court does not believe that utilization of both sections in a series of interrelated transactions makes liquidation under § 731 a sham, rather it enables a retiring partner to delay recog-

nition even though the income-producing or investment property which he acquires from the partnership is not the particular property he wishes to hold on a long-term basis. Recognition of this proposition is implicit in the following statement from *Merten's Law of Income Taxation:*

> "It is possible for gain to be realized by a distributee of partnership property upon the liquidation of a partnership [interest] where there is a simultaneous disposition by him of property distributed. *The gain, however, is realized with respect to the disposition of the property, not with respect to the distribution.* Thus, where the distributee's interest in a capital asset of the dissolved partnership is sold by him to the other partner in an installment sale, the gain on the sale is realized in the years the payments therefor are received." 6 Merten's Law of Federal Income Taxation, § 35.54 at 186.

[3] We believe this to be an accurate statement of the law as it now stands and we hold as a matter of law that Frances Wilson, as retiring partner, received for the partnership in liquidation of her entire partnership interest a liquidating distribution of income-producing property which she subsequently exchanged for property of a like-kind under 26 U.S.C. § 1031. Both transactions had the effect of postponing recognition of capital gains.

Accordingly, plaintiffs' motion for summary judgment is granted.

OPINION OF THE COURT OF APPEALS
(October 22, 1971)

No. 30798

UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

EMORY K. CRENSHAW, as Executor of the
ESTATE OF FRANCES WOOD WILSON, Deceased,
Plaintiff-Appellee,

vs.

UNITED STATES OF AMERICA
Defendant-Appellant.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF GEORGIA

Before BROWN, *Chief Judge*, COLEMAN and CLARK, *Circuit Judges.*

BROWN, *Chief Judge:* In this hotly contested suit for refund of Federal income taxes an ingenious taxpayer and a skeptical tax collector vigorously dispute the legal characterization of an imaginative financial maneuver. If the elaborate multi-stage transaction in question amounted to no more than a "sale or exchange" of a partnership interest under § 741[1] of the Internal Revenue Code of 1954, the Commissioner properly assessed and collected a

[1] "RECOGNITION AND CHARACTER OF GAIN OR LOSS ON SALE OR EXCHANGE.

In the case of a sale or exchange of an interest in a partnership, gain or loss shall be recognized to the transferor partner. Such gain or loss shall be considered as gain or loss from the sale or exchange of a capital asset, except as otherwise provided in section 751 (relating to unrealistic receivables and inventory items which have appreciated substantially in value)." 26 U.S.C.A. § 741.

$47,128.92 deficiency. On the other hand, if it was merely a "liquidating distribution" of a partnership interest governed by § 736 (b)[2], the District Court correctly granted Taxpayer's motion for summary judgment. Initially we encountered some difficulty with the facts because the Government, while relying upon the well-entrenched "step transaction" doctrine, failed to prove all the steps. Now, with that problem solved and the material facts undisputed, we reverse.

Like most sophisticated schemes for minimizing taxes, the plan was an intricate one. It originated in 1962 while Taxpayer (Mrs. Frances Wood Wilson) was the owner of an undivided 50/225 interest in the Pine Forest Associates partnership, the remaining interests belonging to Mr. and Mrs. Leon Blair. Mr. Blair approached Taxpayer's attorney with an offer to purchase her partnership interest for cash, and although this proposal was not generally objectionable the attorney responded by pointing out that Taxpayer's general financial position suggested the most appropriate course would be the exchange of her interest for other income-producing property, rather than for cash.

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[2] "PAYMENTS TO A RETIRING PARTNER OR A DECEASED PARTNER'S SUCCESSOR IN INTEREST.

* * * * *

(b) *Payments for Interest In Partnership.* —

(1) *General rule.* — Payments made in liquidation of the interest of a retiring partner or a deceased partner shall, to the extent such payments (other than payments described in paragraph (2)) are determined, under regulations prescribed by the Secretary or his delegate, to be made in exchange for the interest of such partner in partnership property, be considered as a distribution by the partnership and not as a distributive share or guaranteed payment under subsection (a)." 26 U.S.C.A. §736(b).

Section 761 (*d*) defines "liquidation of a partner's interest" as "the termination of a partner's entire interest in a partnership by means of a distribution, or series of distributions, to the partner by the partnership."

Mr. Blair did not then own such property, but subsequent investigation revealed that it could be obtained from the estate of Taxpayer's husband. The stage was then set for the following planned, integrated sequence of steps:

(i) Taxpayer withdrew completely from the partnership in exchange for an undivided 50/225 interest in a parcel of real estate (the Pine Forest Apartments) owned by the partnership.

(ii) Acting individually and as executrix of her husband's estate, Taxpayer then exchanged her interest in the Pine Forest Apartments for other real property (the Oglethorpe Shopping Center) belonging to the estate.

(iii) Acting solely in her capacity as executrix, Taxpayer transferred the estate's interest in the Pine Forest Apartments for $200,000 cash to the Blair's newly erected closely held corporation (the Blair Investment Company).

(iv) Finally, the Blair Investment Company transferred its 50/225 interest in the Pine Forest Apartments to the partnership in exchange for the partnership interest formerly owned by Taxpayer.[3]

The Government argues that the ultimate consequence of these steps was in every material respect equiva-

[3] In its order granting Taxpayer's motion for summary judgment the District Court stated that all steps took place on November 30, 1962. However, there is no evidence in the record establishing either the existence or timing of the fourth step, and the only reference to it is in the deposition of Mr. Blair's accountant, who stated that he was not present at the closing on November 30, that he did not know whether all the transactions took place on the same day, but that he "assumed" they did. This led to our post-argument request that the parties stipulate the missing facts regarding this step.

Fortunately the gap in the factual landscape was filled by the stipulation that "the Blair Investment Company transferred its interest in the Pine Forest Apartments to the Pine Forest Associates partnership, and that such transfer took place no later than January 31, 1963, as shown by the partnership return of the Pine Forest Associates filed for its fiscal year ending on that date."

lent to that which would have resulted from a taxable sale. The partnership continued to own the same interest in the Pine Forest Apartments that it had purported to distribute in liquidation of Taxpayer's partnership interest, while the Blairs acquired Taxpayer's partnership interest in return for a $200,000 cash outlay. On the other hand, Taxpayer contends that the entire transaction was nothing more than a perfectly legitimate tax-free liquidation followed by an equally legitimate tax-free exchange of like-kind property under § 1031, and that it must therefore be governed by the long-established rule that a taxpayer may properly take advantage of any method allowed by law to avoid taxes. *Rupe Investment Corp. v. Commissioner*, 5 Cir., 1959, 266 F.2d 624, 629.

The critical significance of step (iv) grows out of the two parallel assertions implicit in the Government's theory of the case. First, as has long been recognized, the substance rather than the form of a transaction determines its tax consequences, particularly if the form is merely a convenient device for accomplishing indirectly what could not have been achieved by the selection of a more straightforward route.[4] "To permit the true nature of a transaction to be disguised by mere formalisms, which exist solely to alter tax liabilities, would seriously impair the effective administration of the tax policies of Congress." *Commissoner v. Court Holding Co.*, 1945, 324 U.S. 331, 334, ___ S.Ct. ___, ___, 89 L.Ed. 981, 985. Transparent devices

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[4] Commissioner v. Tower, 1946, 327 U.S. 280, 288-89, ___ S.Ct. ___, ___, 90 L.Ed. 670, 676-77; Helvering v. Clifford, 1940, 309 U.S. 331, ___ S.Ct. ___, 84 L.Ed. 788; Higgins v. Smith, 1939, 308 U.S. 473, 476-77, ___ S.Ct. ___, ___, 84 L.Ed. 406, 410; Griffiths v. Helvering, 1939, 308 U.S. 355, 357-58, ___ S.Ct. ___, ___, 84 L.Ed. 319, 322; Minnesota Tea Co. v. Helvering, 1938, 302 U.S. 609, 613-14, ___ S.Ct. ___, ___, 82 L.Ed. 474, 477; Gregory v. Helvering, 1935, 293 U.S. 465, 470, ___ S.Ct. ___, ___, 79 L.Ed. 596, 599.

totally devoid of any non-tax significance to the parties[5] cannot pass muster even though a literal reading of the statutory language might suggest otherwise. *Commissioner v. P. G. Lake Inc.*, 1958, 356 U.S. 260, 266-67, 78 S.Ct. 691, ___, 2 L.Ed.2d 743, 749. The tax policy of the United States is concerned with realities rather than appearances, and when an illusory facade is constructed solely for the purpose of avoiding a tax burden the astute taxpayer cannot thereafter claim that a court is bound to treat it as being a genuine business arrangement. See *Casner v. Commissioner*, 5 Cir., 1971, ___ F.2d ___ [No. 29290, September 27, 1971, slip op. pp. 40-44].

A corollary proposition, equally well established, is that the tax consequences of an interrelated series of transactions are not to be determined by viewing each of them in isolation but by considering them together as component parts of an overall plan. *Scroll, Inc. v. Commissioner*, 5 Cir., 1971, ___ F.2d ___ [No. 29207, August 13, 1971]; *Waterman S.S. Corp. v. Commissioner*, 5 Cir., 1970, 430 F.2d 1185, 1193-94, *cert. denied*, 1971, ___ U.S. ___, ___ S.Ct. ___, 28 L.Ed2d 219; *Redwing Carriers, Inc. v. Tomlinson*, 5 Cir., 1968, 399 F.2d 652, 658; *Davant v. Commissioner*, 5 Cir., 1966, 366 F.2d 874, *cert. denied*, 1967, 386 U.S. 1022, 87 S.Ct. 1370, 18 L.Ed.2d 460; *Kinney v. United States*, 5 Cir., 1966, 358 F.2d 739; *United States v. General Geophysical Co.*, 5 Cir., 1961, 296 F.2d 86, *cert. denied*,

[5] In arguing that the technical form of the transaction must prevail here, Taxpayer has not once suggested any conceivable legitimate business purpose that might have dictated the utilization of such a convoluted sequence of preplanned paper exchanges in place of a direct sale for cash. See Knetsch v. United States, 1960, 364 U.S. 361, 81 S.Ct. 132, 5 L.Ed.2d 128. Indeed, Mr. Blair told the Board of Directors of the Blair Investment Corporation that the entire elaborate arrangement was "in net effect the same as his proposal." Mr. Blair's view of the transaction coincides with our own — in every respect except its form it was a sale of the partnership interest rather than a liquidating distribution.

1962, 369 U.S. 849, 82 S.Ct. 932, 8 L.Ed.2d 8; *Kanawha Gas & Utilities Co. v. Commissioner*, 5 Cir., 1954, 214 F.2d 685, 691. Taken individually—or a few, but not all, steps at a time—each step in the sequence may very well fit neatly into an untaxed transactional compartment. But the individual tax significance of each step is irrelevant when, considered as a whole, they all amount to no more than a single transaction which in purpose and effect is subject to the given tax consequence.

Here the successful application of these principles depends upon a showing by the Government that, while in form these transfers may appear to be no more than a liquidation of a partnership interest followed by a tax-free § 1031 exchange,[6] in substance they are really nothing more than a camouflaged sale of a partnership interest masquerading as a liquidation. But in order to reach this conclusion it must be shown that the character of the transaction is in every respect, other than the superficial and irrelevant one of form, a sale, resulting in precisely those consequences that would have occurred had Taxpayer simply sold her interest in the partnership to the partnership or to the surviving partners for $200,000 cash and then purchased with that money her income-producing property. And it would be an equivalent transaction if the relative positions of the parties following this well-engineered series of exchanges was for all practical purposes substantially the same as it would have been had they chosen the direct rather than the circuitous route.

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[6] As an alternative ground for reversal the Government argues that the District Court improperly held Taxpayer's exchange of her interest in the apartments for the shopping center to be entitled to the nonrecognition of gain or loss treatment afforded by § 1031, since the apartment property was encumbered by substantial liabilities from which Taxpayer had been relieved. However, since this contention was never presented to the District Court, we do not consider it now.

Obviously what happened here was not equivalent to a sale unless the final step (iv) was consummated—that is, unless Mrs. Wilson's undivided 50/225 interest in the Pine Forest Apartments ultimately found its way back into the partnership now owned by the two Blairs. If it had not, Taxpayer's partnership interest would have been "liquidated," in every conceivable sense of that term, and the complete obliteration of it simply could not have been characterized as a "sale" if none of it had survived to be "sold."

However, the partnership interest *did* survive because, as the parties have stipulated (see note 3, *supra*), it was transferred to the Blair Investment Company in return for its undivided interest in the Pine Forest Apartments. In return for its $200,000 cash payment the corporation (Blair Investment) received exactly the partnership interest it would have obtained by way of a direct purchase from Taxpayer. A sale, not a "liquidation," occurred because what had formerly been Taxpayer's partnership interest was acquired by the Blairs' corporate alter ego and the relative economic positions of the parties were the same as they ultimately would have been had a direct sale taken place.

Moreover, the fact of the eventual transfer of the corporation's undivided interest in the Pine Forest Apartments back into the partnership is of crucial evidentiary significance in the final analysis of whether the essence of the arrangement was a "sale" or "liquidation." For while the proper characterization of the transaction may depend upon whether the participants intended to effect a sale or a liquidation, that intention cannot be conclusively presumed merely because the tax-conscious litigant attaches a particular label to his actions. "If the 'sale' is a sham it will be disregarded and a true sale is not made a liquidation by mere words." *Miller v. United States*, Ct. Cl., 1967,

181 Ct. Cl. 331, 344, n. 3. In short, merely calling the scheme a liquidation does not make it one.

What does, instead, make the transaction in question a sale is the fact that while theoretically a matter of indifference to Taxpayer, consummation of the step (iv) was practically essential to its success, since without it there might have been no deal. Mr. Blair wanted Taxpayer's partnership interest, and to get it he was willing to go along with a suggested alternative plan which he thought amounted to practically the same thing as a direct sale (see note 5, *supra*). The key was to keep Pine Forest Apartments in the partnership. From the partnership's standpoint, this goal would have been frustrated by transferring (and *keeping*) 50/225 of it in the separate corporate entity, a result which might have brought about substantial tax disadvantages. From Taxpayer's standpoint, she needed (or desired) income-producing properties which she could not get from the partnership in a liquidating distribution. To acquire such property (Oglethorpe Shopping Center) she needed cash to pay the seller.[7] But it was disadvantageous for her to get the cash on distribution from the partnership. This cash came through the payment of $200,000 by the corporation for the Pine Forest Apartments interest, which soon got back to the partnership exactly as it all began. And her partnership interest was then owned by the Blairs. Taxwise, taking two to tango, the transaction had to have the equivalent of step (iv) as an indispensable ingredient. The District Court was therefore correct in holding there to be no material issue of fact in controversy, since whether Taxpayer was conscious of step (iv) or not was irrelevant.

Our conclusion is not affected by the undisputed fact that Taxpayer disposed of her entire partnership interest

[7] It is just a coincidence that she was both the willing buyer and the willing seller.

rather than a portion of it. The steps with which we are concerned are those that lead inevitably to a result in every respect equivalent to a taxable sale, even through *individually* any one step may have the technical form of a § 736 liquidation. A step transaction is not magically transformed into something else merely because one of the critical steps was not further subdivided into a piecemeal disposition of the partnership interest, and it makes no difference that following the initial transfer involved in step (i) Taxpayer ostensibly retained no interest whatever. The entire transaction on paper may have been flawless, but it was nevertheless a sale after all was said and done.[8]

Nor do we overlook Taxpayer's clearly correct contention that Congress, in enacting these provisions, has provided an individual with alternative methods for divesting himself of a partnership interest. See *Foxman v. Commissioner*, 3 Cir., 1965, 352 F.2d 466; *Paul J. Kelly*, 1970, 29 T.C.M. 1090; *Andrew O. Stilwell*, 1966, 46 T.C. 247. Taxpayers have a choice between selling and liquidating. But they cannot compel a court to characterize the transaction solely upon the basis of a concentration on one facet of it when totality of circumstances determines its tax status. The most obvious answer to Taxpayer's argument that the parties' characterization is conclusive is that such a result would completely thwart the Congressional policy to tax transactional realities rather than verbal labels. The tax is realized on the sale of a partnership interest, and it cannot be avoided by the simple expedient of constructing an admittedly clever series of successive transfers, each non-taxable in itself, that together work the same result.

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[8] "A given result at the end of a straight path is not made a different result because reached by following a devious path." Minnesota Tea Co., *supra*, 302 U.S. at 613, S.Ct. at , 82 L.Ed. at 477.

Otherwise form, rather than substance, would invariably prevail.

The judgment of the District Court is reversed and the cause remanded for entry of judgment in favor of the United States.

REVERSED and REMANDED.

ORDER OF THE COURT OF APPEALS DENYING PETITION FOR REHEARING AND PETITION FOR REHEARING EN BANC

(January 14, 1972)

UNITED STATES COURT OF APPEALS

FOR THE FIFTH CIRCUIT

No. 30798

EMORY K. CRENSHAW, as Executor of the Estate of Frances Wood Wilson, Deceased,
Plaintiff-Appellee,

vs.

UNITED STATES OF AMERICA
Defendant-Appellant.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF GEORGIA

Before BROWN, *Chief Judge,* COLEMAN and CLARK, *Circuit Judges.*

PER CURIAM: The Petition for Rehearing is DENIED and no member of this panel nor Judge in regular active service on the Court having requested that the Court be polled on rehearing en banc, (Rule 35 Federal Rules of Appellate Procedure; Local Fifth Circuit Rule 12) the Petition for Rehearing En Banc is DENIED.

ORDER OF THE DISTRICT COURT ADOPTING MANDATE OF THE COURT OF APPEALS

(January 26, 1972)

Civil Action No. 12,392

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF GEORGIA

EMORY K. CRENSHAW, as Executor of the Estate of Frances Wood Wilson, Deceased,

vs.

UNITED STATES OF AMERICA

ORDER

Mandate of the U.S. Court of Appeals read and considered.

IT IS ORDERED that the mandate be and it hereby is made the judgment of this Court.

This 27th day of January, 1972.

NEWELL EDENFIELD
United States District Judge

INTERNAL REVENUE CODE OF 1954 (26 U.S.C.)

Sec. 731. Extent of Recognition of Gain or Loss on Distribution.

(a) *Partners.*—In the case of a distribution by a partnership to a partner—

(1) gain shall not be recognized to such partner, except to the extent that any money distributed exceeds the adjusted basis of such partner's interest in the partnership immediately before the distribution, and

* * * *

Sec. 736. Payments to a Retiring Partner or a Deceased Partner's Successor in Interest.

* * * *

(b) *Payments for Interest in Partnership.*—

(1) *General rule.*—Payments made in liquidation of the interest of a retiring partner or a deceased partner shall, to the extent such payments (other than payments described in paragraph (2)) are determined, under regulations prescribed by the Secretary or his delegate, to be made in exchange for the interest of such partner in partnership property, be considered as a distribution by the partnership and not as a distributive share or guaranteed payment under subsection (a).

Sec. 741. Recognition and Character of Gain or Loss on Sale or Exchange.

In the case of a sale or exchange of an interest in a partnership, gain or loss shall be recognized to the transferor partner. Such gain or loss shall be considered as gain or loss from the sale or exchange of a capital asset, except as otherwise provided in section 751 (relating to unrealized receivables and inventory items which have

appreciated substantially in value).

Source: New.

Sec. 761. Terms Defined.

* * * *

(d) *Liquidation of a Partner's Interest.*—For purpose of this subchapter, the term "liquidation of a partner's interest" means the termination of a partner's entire interest in a partnership by means of a distribution, or a series of distributions, to the partner by the partnership.

Sec. 1031. Exchange of Property held for Productive Use or Investment.

(a) *Nonrecognition of Gain or Loss From Exchanges Solely in Kind.*—No gain or loss shall be recognized if property held for productive use in trade or business or for investment (not including stock in trade or other property held primarily for sale, nor stocks, bonds, notes, choses in action, certificates of trust or beneficial interest, or other securities or evidences of indebtedness or interest) is exchanged solely for property of a like kind to be held either for productive use in trade or business or for investment.

TREASURY REGULATIONS ON INCOME TAX (26 C.F.R.)

§ 1.736-1. Payments to a retiring partner or a deceased partner's successor in interest.

(a) *Payments considered as distributive share or guaranteed payment.* (1) (i) Section 736 and this section apply only to payments made to a retiring partner or to a deceased partner's successor in interest in liquidation of such partner's entire interest in the partnership. See section 761(d). Section 736 and this section do not apply

if the estate or other successor in interest of a deceased partner continues as a partner in its own right under local law. Section 736 and this section apply only to payments made by the partnership and not to transactions between the partners. Thus, a sale by partner A to partner B of his entire one-fourth interest in partnership ABCD would not come within the scope of section 736.

* * * *

(b) *Payments for interest in partnership.* (1) Payments made in liquidation of the entire interest of a retiring partner or deceased partner shall, to the extent made in exchange for such partner's interest in partnership property (except for unrealized receivables and good will as provided in subparagraphs (2) and (3) of this paragraph), be considered as a distribution by the partnership (and not as a distributive share or guaranteed payment under section 736(a)).

* * * *

§ 1.1031(a)-1. **Property held for productive use in trade or business or for investment.**

(a) Section 1031 (a) provides an exception from the general rule requiring the recognition of gain or loss upon the sale or exchange of property. See section 1002 and the regulations thereunder. Under Section 1031(a), no gain or loss is recognized if property held for productive use in trade or business or for investment is exchanged solely for property of a like kind to be held either for productive use in trade or business or for investment. Under section 1031 (a), property held for productive use in trade or business may be exchanged for property held for investment. Similarly, property held for investment may be exchanged for property held for productive use in trade or business.

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No. 71-1316

In the Supreme Court of the United States

OCTOBER TERM, 1971

EMORY K. CRENSHAW, AS EXECUTOR OF THE ESTATE OF FRANCES WOOD WILSON, DECEASED, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

ERWIN N. GRISWOLD,
Solicitor General,
SCOTT P. CRAMPTON,
Assistant Attorney General,
RICHARD W. PERKINS,
RICHARD FARBER,
Attorneys,
Department of Justice,
Washington, D.C. 20530.

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OPINIONS BELOW

The opinion of the district court (Pet. App. 19-26) is unofficially reported at 70-2 U.S.T.C., par. 9530. The opinion of the court of appeals (Pet. App. 27-36) is not yet officially reported.

JURISDICTION

The court of appeals on October 22, 1971, reversed the judgment of the district court and remanded the cause for entry of judgment in favor of the United States (Pet. App. 27, 36). A petition for rehearing and petition for rehearing *en banc* were denied on January 14, 1972 (Pet. App. 37). The petition for a

writ of certiorari was filed on April 13, 1972. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether the court of appeals correctly held that a planned series of transactions whereby petitioner [1] withdrew from a partnership constituted a taxable sale of her partnership interest to the remaining partners under Section 741 of the Internal Revenue Code of 1954 rather than a nontaxable liquidation of her interest by the partnership under Section 736(b).

STATUTES AND REGULATIONS INVOLVED

The pertinent provisions of the Internal Revenue Code of 1954 and the Regulations thereunder are set forth in the appendix to the petition (pp. 39–41).

STATEMENT

Petitioner, in November 1962, was the owner of a 50/225 interest in the Pine Forest Associates partnership. The remaining partnership interests were owned by Leon Blair and his wife Julien. Mr. Blair contacted the petitioner's attorney with an offer to purchase her interest for cash, and in response to this offer, the attorney informed Mr. Blair that the petitioner was willing to dispose of her interest, but that, in view of her general financial position, an exchange of the interest for other income-producing property would be more in accord with her needs than a sale.

[1] Decedent, Frances Wood Wilson, is referred to herein as "petitioner."

(Pet. App. 28.) Although Mr. Blair did not then own property suitable for this purpose, subsequent discussions revealed that a suitable piece of property could be obtained from the estate of the petitioner's husband. A plan was then formulated, the end result of which would provide the petitioner with income-producing property, while retaining in the partnership the undivided 50/225 interest in certain property (The Pine Forest Apartments) purportedly distributed to petitioner in liquidation of her partnership interest (Pet. App. 29). Thereafter, in accordance with that plan, the following events occurred (Pet. App. 29):

(1) Petitioner withdrew from the partnership in exchange for an undivided 50/225 interest in a parcel of real estate (Pine Forest Apartments) owned by the partnership;

(2) Acting individually and as executrix of her husband's estate, petitioner transferred the undivided 50/225 interest in the Pine Forest Apartments for other real estate (Oglethorpe Shopping Center) belonging to the estate;

(3) Acting as executrix of her husband's estate, petitioner transferred the undivided 50/225 interest in the Pine Forest property to a new corporation (Blair Investment Company, all of whose stock was owned by Mr. and Mrs. Blair) for $200,000 cash; and

(4) The Blair Investment Company then retransferred the undivided 50/225 interest in the Pine Forest property back to the partnership in exchange

for the partnership interest formerly owned by the petitioner.[2]

On her income tax return for the taxable year 1962, petitioner treated the above-described transactions as a nontaxable distribution of partnership property in liquidation of her partnership interest under Sections 731 and 736(b) of the 1954 Code, followed by a tax-free exchange of the property distributed for other income-producing property. The Commissioner determined a deficiency on the ground that the claimed liquidating distribution was in substance a taxable sale of her interest to the remaining partners pursuant to Section 741 of the Code. (Pet. App. 27–28.) The district court granted summary judgment for the petitioner, holding as a matter of law that the transactions here involved resulted in a nontaxable distribution in liquidation of petitioner's partnership interest (Pet. App. 26). On appeal, the Fifth Circuit held that the tax consequences of the interrelated series of transactions could not be determined by viewing each transaction in isolation, but instead required consideration of each step as a component part of an overall plan (Pet. App. 31). Applying that standard, the court of appeals noted that the transactions here were so designed that petitioner's undivided 50/225 interest in the Pine Forest Apartments ultimately found its way back into the partnership now owned by the Blairs, and held that, since

[2] The first three transactions all took place on November 30, 1962. The exact date of the fourth transaction is unknown; it was stipulated, however, in the court of appeals that it took place no later than January 31, 1963. (Pet. App. 29.)

this step was an indispensable ingredient in the overall plan, the entire transaction constituted a sale rather than a Section 736 liquidation (Pet. App. 33–35).

ARGUMENT

The decision below is correct. There is no conflict of decisions or any other reason for further review by this Court.

1. In holding that the substance of the planned series of transactions whereby the petitioner withdrew from the Pine Forest partnership was a taxable sale of her partnership interest to the remaining partners, the court of appeals reached the only conclusion compatible with the uncontroverted facts of this case. Section 741 of the Internal Revenue Code of 1954 (Pet. App. 39–40) provides that the gain or loss on a sale or exchange of an interest in a partnership shall be recognized by the transferor partner. On the other hand, Section 736(b) of the Code (Pet. App. 39) provides that payments to a partner by a partnership in liquidation of the partner's interest are considered to be a distribution by the partnership and as such are (with certain exceptions not applicable here) nontaxable under Section 731(a) (Pet. App. 39). "Liquidation of a partner's interest" is defined in Section 761(d) (Pet. App. 40) as the termination of a partner's entire interest by means of a distribution by the partnership to the partner. Thus, the distinction between Section 741 and Section 736 is that the latter provision applies only to payments made by the partnership in exchange for the partnership interest of a retiring partner and does not apply to transac-

tions between the partners. See Treasury Regulations § 1.736–1(a) (Pet. App. 40–41).

The court of appeals correctly concluded that, in substance, the petitioner sold her interest to Mr. and Mrs. Blair. At the end of the series of integrated transactions, the partnership property purportedly distributed to petitioner in liquidation of her interest was back in the partnership and the continuing partners, through their wholly owned corporation, had, in effect, purchased petitioner's interest for $200,000 cash.[3] Simply stated, there were no payments (and hence no liquidating distribution) by the *partnership* and therefore no basis for the application of Section 736(b). The round-robin transfer of the Pine Forest property from the partnership to the petitioner, to the estate of her husband, to the Blair corporation, and back to the partnership was, as the Court of Appeals properly held, merely a facade erected to disguise the true nature of the transaction. See *Commissioner* v. *Court Holding Co.*, 324 U.S. 331; *Minnesota Tea Co.* v. *Helvering*, 302 U.S. 609; *Waterman Steamship Corp.* v. *Commissioner*, 430 F. 2d 1185 (C.A. 5), certiorari denied, 401 U.S. 939; *United States* v. *General Geophysical*, 296 F. 2d 86 (C.A. 5), certiorari denied, 369 U.S. 849.

Petitioner asserts (Pet. 7–8) that the holding of the court below subverts the Congressional policy with respect to the tax treatment of retiring partners. There is no question that, in enacting Sections 736

[3] Under this theory, of course, petitioner would be deemed to have purchased the property from her husband's estate with the $200,000.00 paid to her by Mr. and Mrs. Blair.

and 741 and the other partnership provisions as part of the Internal Revenue Code of 1954, Congress intended to allow partners to decide among themselves whether a partner's withdrawal from a partnership shall be by the "sale" route or the "liquidation" route. Indeed, the court of appeals expressly acknowledged (Pet. App. 35) the right of partners to choose between selling and liquidating. In the instant case, however, petitioner's tax difficulties arose solely from her unwillingness, for economic considerations which she deemed important, to make a straight-forward transfer of her partnership interest in exchange for payments from the partnership in liquidation of that interest; instead, she chose to be paid, in effect, by the individual partners. Accordingly, the court of appeals correctly recognized that the tax consequences of petitioner's withdrawal depended upon the route which the parties actually took, and not upon the label which petitioner seeks to attach to the transactions.

2. The holding of the court below is not in conflict with the decision of the Third Circuit in *Foxman* v. *Commissioner*, 352 F. 2d 466, as petitioner contends (Pet. 6–8). Indeed, *Foxman* is entirely consistent with the decision here. *Foxman* involved payments made to a retiring partner in the form of checks and notes issued by the partnership, undr circumstances where it was to the tax advantage of the continuing partners to have the transaction treated as a liquidation of the interest of the retiring partner, but such liquidation treatment would have resulted in adverse tax consequences to the retiring partner. In that case, the continuing partners argued that since the payments to the retiring

partner were made in the form of checks and notes issued by the partnership, the transaction must be treated for tax purposes as a Section 736 liquidation. The court of appeals rejected this argument as unduly emphasizing form over substance, in contravention of this Court's decision in *Commissioner* v. *Court Holding Co., supra*. The court went on to affirm the Tax Court's decision that, in substance, the payments there in question were made by the remaining partners, and, accordingly the transaction was a sale. Similarly, the Fifth Circuit here has followed the mandate of *Court Holding Co.* in determining that the substance and net effect of the series of integrated transactions was a sale of the petitoner's partnership interest.

3. Petitioner also relies (Pet. 8–13) on cases arising under Section 1031(a) (Pet. App. 40) to establish a basis for review of the decision below. In those cases, the courts have held that certain three-party exchanges of like-kind property involving simultaneous purchases and exchanges qualify for the nonrecognition of gain treatment afforded by Section 1031. The transaction in the present case cannot, however, be characterized as merely a three-cornered exchange of property, as petitioner suggests. Rather, the instant case involves the disposition of the petitioner's partnership interest, the tax consequences of which are controlled by the specific partnership provisions of the Code and not by Section 1031. The issue before the court below was whether the petitioner, in substance, had effected a taxable sale of her interest or a nontaxable liquidation of that interest. That issue cannot be determined by viewing each of the interrelated

transfers in isolation instead of considering them as an integrated whole.[4]

4. Finally, petitioner argues (Pet. 13–18) that the decision below erroneously applied the "substance versus form" doctrine as amplified and explained by this Court in *Commissioner* v. *Court Holding Co., supra,* and *United States* v. *Cumberland Public Service Co.,* 338 U.S. 451. The ultimate question in each of those cases was whether a sale of corporate assets was made by the corporation or by its shareholders in their individual capacity. This Court, in *Court Holding,* affirmed the finding of the Tax Court that the substance of the transaction was a sale by the corporation. In reaching its decision, the Court made its well-known statements that the (p. 334) "incidence of taxation depends upon the substance of a transaction" and that tax liabilities cannot be altered by "mere formalisms." The decision in *Cumberland,* affirming the finding of the Court of Claims that the transaction there was a sale by the shareholders, did not retreat from the legal principles in *Court Holding,* as petitioner suggests. Rather, the court merely pointed out (pp. 454–455) that its language in *Court Holding* did not mean that a corporation could be taxed even where the sale has been made by its stockholders following a *genuine* liquidation and dissolution. The uncontroverted facts here establish that the court of appeals correctly concluded, consistent with

[4] The petitioner's allegation (Pet. 10) that the decision below is in conflict with other decisions of the Fifth Circuit is without foundation. In any event, intra-circuit conflict is not a valid ground for review by this Court. See *Wisniewski* v. *United States,* 353 U.S. 901.

the *Court Holding* and *Cumberland* decisions; that there was no genuine liquidation of petitioner's partnership interest.

CONCLUSION

The petition for certiorari should be denied.

Respectfully submitted.

ERWIN N. GRISWOLD,
Solicitor General.
SCOTT P. CRAMPTON,
Assistant Attorney General.
RICHARD W. PERKINS,
RICHARD FARBER,
Attorneys.

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